

November 8, 2012

MEMORANDUM

TO: Executive Agency Heads
CC: Cabinet Secretaries
FROM: Martin L. Kent, Chief of Staff
SUBJECT: Budget Reduction Strategies

As the Governor and his Finance team continue the process of budget development in advance of the 2013 session of the General Assembly, it has become clear that several factors are placing immense pressure on the Commonwealth's finances and, therefore, will necessitate immediate action to plan prudently for the future. Foremost among them is the unprecedented uncertainty in Washington and its detrimental effects on this state. The so-called fiscal cliff in the third quarter of FY2013, including the sequestration provision of the Budget Control Act of 2011, could touch off an economic retraction or even a second recession. National economists have down-played any expectations of a near-term, vigorous recovery and confirmed the direct connection between the existing economic uncertainty and the potential for future revenue stagnation or losses. In the face of this uncertainty, it is our constitutional responsibility to prepare for the associated risk.

The rising cost of health care will appear within this budget in several forms. First, statewide Medicaid costs will further strain budget resources in the coming year. Medicaid is second only to K-12 education as the largest driver in the state budget and comprises approximately 20 percent of the general fund budget; mandatory growth in the program will demand significant, additional resources. Further, additional health care cost increases are presenting themselves within the employee health insurance program and the cost of providing inmate medical care. Balances sufficient to cover this continued growth do not exist.

On the revenue side, nearly all of the FY2012 budget surplus has been spoken for by constitutionally or statutorily required deposits (e.g., to the Revenue Stabilization Fund and the Water Quality Improvement Fund) or by the bonus to be paid on December 1st. Most, if any, new revenue growth was anticipated in the revenue forecasts adopted last year and, therefore, already have been programmed into the budget. Any new growth likely will be limited.

As a member of the Governor's leadership team, I know that you have followed these matters closely, and that none of this information comes as a surprise. I reiterate it because, based on the foregoing, I must ask for the following from each executive branch agency:

By no later than November 21, 2012, please prepare for the Governor's review savings strategies for FY 2014 equal to four (4) percent of your agency's legislative general fund appropriation.

Your respective analyst in the Department of Planning and Budget will contact you with any

adjustments to your reduction base and the exact reduction target for your agency.

We understand that the ongoing hiring freeze has placed additional responsibilities on state employees. Therefore, as has been asked annually as part of your ongoing efficiency reviews, these savings plans should focus on identifying the lowest priority activities in your respective agency, rather than on personnel. To the extent you have submitted a savings strategy in a prior year of this Administration and it has not been accepted, please do not resubmit it.

While we welcome any and all valid savings strategies, it is important that the majority of your reduction strategies emphasize recurring savings rather than one-time savings. Additionally, you should not submit reduction strategies that simply pass or add additional costs to another state agency or that reduce revenue to another state agency. Please specifically look at service and program areas where state funds are used to match federal funds or other nongeneral funds. You need to ask if the use of these funds, state and federal, is achieving outcomes that are of the highest priority for use of the general fund match. You should not consider these programs as "off-limits" for savings and efficiency strategies just because they may result in the loss of matching funds.

Please also focus on strategies that call for the modification or elimination of existing responsibilities that have been placed on you that are not mission critical for your agency. Ask your policy or appropriate liaison to meet with the Governor's Policy Office to discuss any necessary statutory amendments to remove such requirements from the Code of Virginia.

Because of the very short timeframe within which we must act on these strategies, please ensure that your recommendations are both practical and consistent with known priorities or directives of the Governor. To the extent an agency submits a savings strategy that does not meet these criteria, the Governor may reduce that agency's base appropriation after consultation with the Department of Planning and Budget.

Your final plans must be submitted in DPB's performance budgeting system and are due no later than **November 21, 2012**. DPB will issue guidance for this submission later today. This timeframe is necessary so that the Governor has sufficient time to appropriately evaluate these strategies for inclusion in his budget to be submitted in December, should such savings become necessary. (NOTE: These plans will be considered official budget submissions and, as such, will be sent to the General Assembly within five (5) days of receipt by DPB. They will also be available to the public and media.)

Institutions of higher education are not included for purposes of this memo, but will be addressed in a separate communication.

Thank you for your continued efforts in governing the Commonwealth in a time of great economic uncertainty. The Governor and I appreciate your service to the public and your continued support to make Virginia the best place to live and work.